Supreme Court, U.S.
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No. 04-163

IN THE

SUPREME COURT OF THE UNITED STATES

LINDA LINGLE,
GOVERNOR OF THE STATE OF HAWAII, *et al.*,
Petitioners,

v.

CHEVRON USA, INC.,
Respondent.

ON WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF *AMICUS CURIAE* OF MANUFACTURED HOUSING COMMUNITIES OF ARIZONA, INC. IN SUPPORT OF RESPONDENT

MICHAEL A. PARHAM
5333 North Seventh Street
Suite B-213
Phoenix, Arizona 85014
(602) 265-6804
Attorney for Amicus Curiae, Manufactured Housing Communities of Arizona, Inc.

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QUESTIONS PRESENTED

1. Whether the Just Compensation Clause authorizes a court to invalidate state economic legislation on its face and enjoin enforcement of the law on the basis that the legislation does not substantially advance a legitimate state interest, without regard to whether the challenged law diminishes the economic value or usefulness of any property.

2. Whether a court, in determining under the Just Compensation Clause whether state economic legislation substantially advances a legitimate state interest, should apply a deferential standard of review equal to that traditionally applied to economic legislation under the Due Process and Equal Protection Clauses, or may instead substitute its judgment for that of the legislature by determining *de novo*, by a preponderance of the evidence at trial, whether the legislation will be effective in achieving its goals.

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INTEREST OF AMICUS CURIAE[1]

This brief is submitted in support of the Respondent herein.

Manufactured Housing Communities of Arizona, Inc. (MHCA) is a statewide organiztion of owners and managers of mobile home parks throughout Arizona. Arizona does not presently allow rent control but in recent years the legislature has considered changing that policy.

The Arizona Mobile Home Parks Residential Landlord and Tenant Act (ARS §33-1401 *et seq.*) which applies to the rental of lots to tenants owning their own mobile homes, creates a "perpetual lease" by preventing a landlord from terminating or refusing to renew an existing tenant's rental agreement without narrowly defined "good cause". ARS §33-1476(B). If a tenant wishes to sell his mobile home on-site, the landlord must permit the purchaser to become a replacement tenant unless he has reasonable cause to disapprove the purchaser's application. ARS §33-1452(D)(3).

Unlike a number of other states including California, the Arizona Act specifically prohibits local rent control, pre-empting that subject to the State. ARS §33-1416-(A). Arizona has not, to date, imposed any controls over what landlords may charge tenants as rent.

In recent years, however, the Arizona legislature has considered bills imposing rent control on mobile home

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[1] Petitioners and Respondent have filed global consents to the filing of all *amicus* briefs in this case. No counsel for a party authored this brief in whole or in part. No persons or entities other than the *amicus* made a monetary contribution to the preparation or submission of this brief.

park landlords. These bills have been sponsored by organizations representing the interests of mobile home park tenants. There are approximately 400,000 people residing in about 2,000 Arizona mobile home parks. In terms of numbers of interested voters in the state, those favoring rent control vastly outnumber those opposed.

This organization, then named the Arizona Mobile Housing Association, Inc., submitted an *Amicus Curiae* brief in 1991 in *Yee v. City of Escondido*, 503 U.S. 519 (1992). It was concerned at that time that the "perpetual lease" alone represented a physical taking. *Yee*, of course, raised the question of whether the "perpetual lease" created by California law coupled with a local rent control ordinance amounted to a physical taking where the result of the combination was the creation of a "premium" in favor of the tenant. Such a premium reflects a transfer of value from landlord to tenant resulting from imposition of rent control.

Yee concluded that a physical taking did not result from these circumstances but left undecided whether the combination of a rent control ordinance with a perpetual lease may amount to a regulatory taking. The MHCA believes that the instant case may well answer that question.

While Arizona still does not have any rent control laws in place, bills creating mobile home park rent control have been gathering greater legislative support as tenants organize to support them. The instant case has the potential of establishing the standards which must be met for a rent control law to satisfy the requirements of the Takings Clause; that is, whether the law merely has some rational basis or, alternatively, whether it must substantially advance a state interest.

MHCA wishes to bring into focus the compelling need for adoption of the latter standard in a situation involving a state with no current rent control but which is now grappling with whether to adopt such legislation.

SUMMARY OF ARGUMENT

Validation of rent control laws as constitutional on a mere showing that they have some rational basis will open the door to their use to accomplish transfers of wealth from landlords to tenants. Only by requiring the government to be prepared to prove that a given law will actually substantially advance a legitimate public purpose can private rental property owners be assured the protections of the Takings Clause.

Rent control is an extraordinary form of government economic regulation justifying a test of whether it substantially advances a legitimate government interest as opposed to whether there is a rational basis in order for the regulation to be held valid under the Takings Clause. Rent control always reduces the value of the regulated party's property. When tenants can transfer leasehold interests to third parties at controlled rents, the result is almost invariably a transfer of wealth from landlord to tenant; the reduction of the value of the landlord's property; and the creation of a premium for the tenant.

The reduction in value of the landlord's property alone, absent any other considerations, amounts to a taking. As such, the test of constitutionality should be whether the regulation substantially advances a legitimate governmental interest. Certainly, where not only the landlord's property value is reduced but a premium is created in the tenant (that is, where a transfer of wealth results from the governmental action between

private parties) the test of constitutionality should be the "substantially advances" test.

ARGUMENT

THE PROPER STANDARD OF REVIEW AS TO WHETHER A RENT CONTROL STATUTE MAY BE DEEMED A TAKING IN VIOLATION OF THE TAKINGS CLAUSE IS WHETHER IT SUBSTANTIALLY ADVANCES A LEGITIMATE GOVERNMENT INTEREST.

In dealing with recent efforts to establish rent control in Arizona, the MHCA has only needed to look west across the Colorado River to see what will happen. Like California, Arizona already has a state law creating the perpetual lease (i.e., ARS §33-1476(B) prohibits non-renewal of an expired mobile home lot lease without narrowly defined good cause and ARS §33-1452(D)-(3) allows the tenant to transfer his leasehold interest in the lot to third parties). Coupling this with a typical California type rent control law could be expected to produce a reduction in the value of the rental lot to the landlord/lot owner, and an increase in the value of the tenant owned mobile home occupying the lot beyond any intrinsic value in the home itself.[2] Common sense indicates that a tenant owning a mobile home on a rental lot not subject to limitations on future rent increases which then falls under government controls prohibiting or limiting future rent increases suddenly owns an asset with greater value, which can be realized when his rights are transferred to third parties.

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[2]Hirsch & Hirsch, *Legal-Economic Analysis of Rent Controls In a Mobile Home Context: Placement Values and Vacancy Decontrol*, 35 UCLA L.Rev. 399. This study examined 344 mobile home sales in 40 California cities, concluding that resale prices exceeded sales price of comparable homes by dealers in cities subject to rent controls.

In California, the result is that benefits for future tenants moving into mobile home parks with controlled below-market rents are offset by the higher prices they must pay to existing tenants to buy their mobile homes. There is, typically, marginal if any benefit to the public. The benefit is to tenants owning homes in mobile home parks at the time the rent control scheme is created. The values of their homes go up. This is offset by the detriment to the landlords who can no longer charge rent the market would otherwise permit. There is no public benefit to justify the harm to landlords.

That situation is similar to the instant case where the weight of the evidence established no public benefit resulting from government control of service station rents. Petitioners argue, however, that the courts have no business "second guessing" a legislative determination that there is a rational basis for the restrictions.

In *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987), the Court established as a standard of review the "substantially advance" test when the statute at issue diminished a landowner's property rights and conferred rights in the landowner's property on private third parties. Most rent control ordinances have this effect, at least when the tenant's leasehold interest in transferable to other parties at controlled rents (the tenant, for purposes of *Nollan* being the third party receiving the rights transferred from the landlord).

This is the basis, in large part, for the Ninth Circuit's decision in the instant case.

In reviewing a California rent control ordinance which unquestionably accomplished a transfer of wealth from a rent controlled mobile home park landlord to the tenants owning mobile homes on its lots, the Court in *Yee*

v. City of Escondido, 503 U.S. 519 (1992), indicated that the "substantially advance" test was the correct standard. *Yee* indicates that not every loss of value to a property owner resulting from governmental rent control will qualify as a taking. To the extent it may constitute a taking, however, it will be treated as a regulatory taking.

It is clear that the standard for review of many, perhaps most economic regulations is the "rational basis" test. That is, the statute will be upheld so long as there is a rational basis for the legislature to conclude that the challenged law advances a legitimate purpose. This test is explained in *FCC v. Beach Communications, Inc.*, 508 U.S. 307 (1993), as one of determining "whether there is any conceivable rational basis justifying (the regulatory scheme) for purposes of the Due Process Clause of the Fifth Amendment". *Beach*, 508 U.S. at 309.

This "rational basis" test has been fairly characterized by one commentator as follows:

> The test of "rationality" is easy to pass: As long as any non-crazy legislator might plausibly believe – based on common speculation, or common sense instinct, with or without benefit of any social science or other data – that a law will make even a small dent in a social problem, the law survives review.

Vikram David Amar, *Rent Control in Hawaii Goes All the Way to the Supreme Court: An Interesting Takings Clause Challenge*, http://writ.news.findlaw.com/amar/-20041103.html.

Whether the government action has a rational basis may be a satisfactory standard when it comes to a review of zoning,[3] or a review of whether only licensed funeral

[3] *Schad v. Borough of Mount Ephraim*, 452 U.S. 61 (1981).

directors will be allowed to sell caskets.[4] But it is not a sufficient test when it comes to reviewing governmental action capping revenues generated by income producing properties thus reducing their values. This is especially true when the ultimate consequence is a transfer of wealth among private citizens.

Rent control can be popular and relatively easy to impose even in the absence of any legitimate justification:

> Polls of economists have found virtually unanimous agreement that declines in product quantity and quality are the usual effects of price controls in general. Of course there are not enough economists in the entire country for their votes to matter very much to politicians, who know that there are always more tenants than landlords and more people who do not understand economics than there are who do. Politically, rent control is often a big success however many serious economic and soeicl problems it creates.

Thomas Sowell, *Basic Economics: A Citizen's Guide to the Economy*, (Basic Books, 2000), page 29.

When the tenant is permitted to transfer the property with the rent unchanged or at least not "de-controlled", the practical effect is to take the landlord's value and give it to the tenant just as surely as if a physical part of the land was transferred. In fact, it's an even better deal for the tenant since in the typical rent control scheme, the landlord still has the duty to maintain the property.[5]

[4] *Craigmiles v. Giles*, 312 F.3d 220 (6th Cir. 2002).

[5] Walter Block, *Rent Control, The Concise Encyclopedia of Economics*, http://www.econlib.org/library/Enc/RentControl.-html, points out that while required to maintain the property,

[footnote continued]

Petitioners have analogized the action of the Ninth Circuit in the instant case to the so-called second guessing test espoused in *Lochner v. New York*, 198 U.S. 45 (1905). The rationale is that by applying the "substantially advance" standard in a rent control case, it follows that the same test will be applied in all cases involving economic regulation. This is not the case nor should it be.

Economic regulation cases are not a "one size fits all" situation. The MHCA certainly does not advocate the "substantially advance" test in all economic regulation situations. But where the effect of the regulation is a fundamental reduction in the value of the regulated party's property, or worse, an actual transfer of wealth from the regulated party (the landlord) to a specific beneficiary of the regulation (the tenant), the test under the Takings Clause should be whether it substantially advances a legitimate governmental interest. Such a distinction would avoid the perceived horrors of a return to the *Lochner* era.

Since the paramount purpose of a revenue producing property such as a mobile home park is establishing and collecting rent, any action by the government eliminating or reducing the owner's ability to do so is a taking of a fundamental property right. In a sense it is worse than taking title to the property since the owner is left with an undiminished obligation to continue to maintain the property.

Restricting this ability to generate revenue is a restriction quite different from other forms of economic regulation. While all have financial consequences and some

landlords frequently lack the means or incentive to do so due to inadequate income.

impact on property values, the imposition of rent control goes to the essence of ownership of rental properties. Landlords regard themselves as owning the right to an income stream, not a piece of land, and terminating or limiting that income stream in reality constitutes a taking of the value of what the owner has.

The Court should recognize this fundamental difference between laws regulating how much cash a revenue producing property is allowed to generate from other restrictions on how land may be used which may have economic consequences, even in cases in which there is no evidence of the creation of a premium in favor of a tenant. Whatever standard must be met in other economic regulation cases, the government should be put to the test of establishing that a rent control regulation substantially advances a legitimate government interest.

The Just Compensation Clause of the Fifth Amendment "represents a paradigmatic American privilege and immunity". Akhil Reed Amar, *The Bill of Rights: Creation and Reconstruction* (Yale University Press, 1998), page 268. By the time Congress drafted the Fourteenth Amendment, just compensation was almost universally considered a fundamental principle of justice. *Id.*

The legislative intent in this area underlying the Fourteenth Amendment was to overturn *Baron v. Baltimore*, 32 U.S. (7 Pet.) 243 (1833); to protect U.S. Citizens "whose property by state legislation had been wrested from them under confiscation". Amar, *The Bill of Rights, supra*, Page 268. This intent is hardly given effect by allowing a state to confiscate part of a revenue stream from an income producing property simply by showing that there may be some rational relationship of its action to a government interest.

Requiring the state to demonstrate that its action substantially advances a legitimate state interest does not constitute second-guessing of economic regulation. It simply puts the government to the task of establishing not only a compelling public purpose but that it will actually be served.

All rent control regulations reduce the value of the landlord's assets, and consequently they should be subject to the "substantially advances" test. But at the least, in those cases in which the evidence demonstrates the probability of a transfer of value from landlord to tenant meaning the tenant will receive a "premium" as the result of the regulation, the "substantially advances" test should apply.

The MHCA and the State of Arizona are at the entrance to a path leading to rent control. All parties need to know what standards Arizona must meet if it chooses to regulate rents. Can it control rents based on unsupported speculation that some worthwhile purpose will be served? Or must it be prepared to establish that the reduction in the landlord's property value and the creation of a premium for the tenant really advance a legitimate government interest.

CONCLUSION

Rent control violates the Takings Clause unless the regulation substantially advances a legitimate government interest.

Respectfully submitted,

MICHAEL A. PARHAM
5333 North Seventh Street
Suite B-213
Phoenix, Arizona 85014
(602) 265-6804
Attorney for Amicus Curiae,
Manufactured Housing
Communities of
Arizona, Inc.

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